

1-1953

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Recommended Citation

John P. Horgan, *Some Legal and Appraisal Considerations in Lease-Hold Valuation under Eminent Domain*, 5 HASTINGS L.J. 34 (1953).
Available at: https://repository.uchastings.edu/hastings_law_journal/vol5/iss1/2

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SOME LEGAL AND APPRAISAL CONSIDERATIONS IN LEASEHOLD VALUATION UNDER EMINENT DOMAIN

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Writing on the subject "Appraising Leasehold Estates" in the October, 1947, issue of *The Appraisal Journal*, Stanley L. McMichael points out that leasehold valuations present intricate problems which call for a high order of judgment, a wealth of experience, and the ability to properly apply mathematical formulae to the end that conclusions and mechanics are so combined that a fair valuation results. McMichael says:

"Establishing a valuation for a leasehold is one of the most difficult and complicated problems that an expert appraiser is called upon to solve. Even for the realtor who has been appraising real estate of all kinds for many years it presents some of the most perplexing questions ever encountered in the valuation field."

It is at least equally true from the point of view of the lawyer who must reconcile, as best he can, a mass of judicial precedent—more often conflicting than not—that the legal aspect of leasehold valuation presents highly complex and sometimes frustrating problems.

The leasehold problem from the lawyer's point of view is not a source of particular concern when the entire fee and all interests therein are condemned at the same time. But the valuation problem will still remain if subsequent litigation develops between landlord and tenant as to their respective shares in the award. The procedure indicated by the California Code of Civil Procedure¹ eliminates separate valuations of component interests and reduces significantly the problems of both the lawyer and the appraiser in the first instance.² It is, rather, in those rare cases where the condemnor separately condemns the fee subject to a leasehold estate and then later proceeds against the lessee to condemn his interest that the legal and appraisal problems become complicated. This is also true in cases where litigation results from failure of the landlord and tenant to agree on their respective shares in the total award.

It is to these situations that many of the considerations which follow will be addressed. It should be emphasized in the beginning that this can

¹§ 1246.1 (Deering 1953.) "(Apportionment of damages among co-owners: Costs of apportionment.) Where there are two or more estates or divided interests in property sought to be condemned, the plaintiff is entitled to have the amount of the award for said property first determined as between plaintiff and all defendants claiming any interest therein; thereafter in the same proceeding the respective rights of such defendants in and to the award shall be determined by the court, jury, or referee and the award apportioned accordingly. The costs of determining the apportionment of the award shall be allowed to the defendants and taxed against the plaintiff except that the costs of determining any issue as to title between two or more defendants shall be borne by the defendants in such proportion as the court may direct."

²*People v. Buellton Development Co.*, 58 Cal.App.2d 178, 136 P.2d 793 (1943); *City of St. Louis v. Rossi*, 333 Mo. 1092, 64 S.W.2d 600 (1933).

in no way be considered a treatise on the subject nor, obviously, can the treatment be assumed exhaustive. It is an attempt to set out guide posts in what surely is a tangled judicial wilderness. An effort is made to deal in fundamentals—some of which have been accepted for many years, more on faith than on annotation. These so-called fundamentals have been fortified with representative case citations in the hope that the reader who may someday be confronted with a leasehold valuation problem will at least find a point of departure for the research which will be necessary. Let him who has the soul of the judicial adventurer blaze further this rough trail hewn into an area of thought where many a lawyer and many an appraiser has ventured and not returned.

Measure of the Compensation

It is fundamental that a lessee is entitled to compensation when all or part of the property leased is taken or damaged through eminent domain during the term of the lease.³ This statement is, of course, subject to the qualification that the leasehold interest has a measurable market value.

It has been held in this state that the interest of a tenant under a lease for a term of years is property subject to ownership and is held as any other interest in land, and subject to the exercise of the power of eminent domain, but the tenant is guaranteed just compensation before his title can be divested under such power if the lease has a market value. It has been held that where the taking is of the *entire* property covered by a lease, the condemnation proceeding operates to release the tenant from liability for subsequently accruing rent, but where the taking is of a *portion* only of the property covered by a lease, the condemnation does not terminate the lease nor absolve the tenant of his covenant to pay the full rent.⁴

Two principal questions concern us here. First, the measure of compensation to which a lessee may be entitled and, secondly, the elements of damage for which a lessee may properly claim compensation. It was held in California in the case of *Kishlar v. Southern Pacific R. Co.*⁵ that the value of the lease at the time of the taking is not its value to the lessee for a particular purpose but its *fair market value*.

The case of *City of Oakland v. Pacific Coast Lumber and Mill Co.*⁶ was an action in eminent domain brought by the City of Oakland to condemn certain waterfront properties. The Oakland Water Front Company had leased to defendant certain of its tidelands on the estuary harbor front in the City of Oakland. The City of Oakland purchased the fee of the property from the Oakland Water Front Company subject to defendant's leasehold

³18 Am.Jur., Eminent Domain § 232.

⁴*City of Pasadena v. Porter*, 201 Cal. 381, 257 Pac. 526 (1927).

⁵134 Cal. 636, 66 Pac. 848 (1901).

⁶171 Cal. 392, 399, 153 Pac. 705 (1915).

interest, and then brought this action to condemn that leasehold interest as to a part of the property so held under lease by defendant. At the time of the commencement of the action the lease had 2 2/3 years to run, with an option of six years renewal. In approving the instructions and rulings of the trial court the Supreme Court says, with reference to the proper measure of the value of a leasehold interest, at page 399:

"And in the case of a leasehold, unless exceptional circumstances are shown, it is held that the value of the lease is its market value. (*Kishlar v Southern Pacific R.R. Co.*, 134 Cal. 636 [66 Pac. 848].)"

Again, in the case of *Los Angeles County v. Signal Realty Co.*⁷ the court, in quoting from a New Hampshire case, approves the statement that in the case of leasehold interests the measure of damages is the market value of the unexpired lease.

It is apparent from the cases in California that this state follows the general rule as to the measure of the value of a condemned leasehold interest. That measure is the difference between the *economic* rent and the *contract* rent. Obviously, if the economic rent, which is the price which could be obtained on a sale of the lease in the open market, is equal to or less than the contract rent provided for in the lease, then the lease has no market value and the ousted tenant has no compensable claim for damages.⁸

In situations where the economic rent exceeds the contract rent, giving a market value to the lease, this excess is sometimes spoken of as the *bonus value* of the lease. More properly, however, it is the market value.

The case of *State of Nebraska v. Platte Valley Public Power & Irrigation District*⁹ holds:

"The general rule is that 'If a leasehold interest is taken, or injured, the lessee is entitled to a sum which will restore the money loss consequent to the taking or injury. This consists generally of the fair market value of the leasehold or unexpired term of the lease, and is said to be the difference between the rental value of the remainder of the term and the rent reserved in the lease.' 29 C.J.S., Eminent Domain, § 143, subsec. b, p. 988."

It has been said in *Corpus Juris Secundum*:

"The test of the value of the lessee's right lies in the excess of the sum for which such right will sell over the amount he has agreed to pay for it by way of rental."¹⁰

⁷86 Cal.App. 704, 712, 261 Pac. 536, 539 (1927).

⁸*Corrigan v. City of Chicago*, 144 Ill. 537, 33 N.E. 746 (1893); *State of Nebraska v. Platte Valley Public Power and Irrigation District*, 147 Neb. 289, 23 N.W.2d 300 (1946); *Board of Chosen Freeholders of Hudson Co. v. Emmerich*, 57 N.J.Eq. 535, 42 Atl. 107 (1898); *Newark v. Cook*, 99 N.J.Eq. 527, 133 Atl. 875 (1926); *Newark v. Eisner*, 100 N.J.Eq. 101, 135 Atl. 86 (1926); *Re William Street*, 19 Wend. 678 (N.Y., 1839); *Bernagozzi v. Mitchell Realty Co.*, 133 Misc. 594, 232 N.Y.Supp. 666 (1929); *Mason v. City of Nashville*, 155 Tenn. 256, 291 S.W. 1074 (1927).

⁹147 Neb. 289, 300, 23 N.W.2d 300, 308, 166 A.L.R. 1196 (1946).

¹⁰29 C.J.S., Eminent Domain § 143(b), n. 71.

In Orgel, *Valuation Under Eminent Domain*, section 124, the author says:

"The formal doctrines adopted in determining compensation for a fee taking are carried over to the valuation of leaseholds, and the courts generally state that the market value of the leasehold is the measure of compensation. It is usually assumed that this market value is equal to the excess of the rental value over the rent reserved. Probably most courts would approve the method of valuation of the leasehold which the Illinois Appellate Court affirmed in *Yellow Cab Co. v. Howard* [243 Ill.App. 263 (1927)] and which the trial court described as follows:

"The dimensions of the premises are 180 feet by 112 feet or 20,160 square feet, at 48 cents per square foot [*the economic rent*] is \$9,676.80 per year. The lease had one year, nine months to run or $1\frac{3}{4}$; \$9,676.80 for $1\frac{3}{4}$ years is \$16,934.40. Rent reserved in lease for $1\frac{3}{4}$ years at \$6,000 per year [*contract rent*] is \$10,500. Deducting \$10,500 from \$16,934.40 is \$6,434.40, or the value of the leasehold. *Yellow Cab Company* is entitled to recover judgment for the sum of \$6,434.40."

Some appraisers might say that the court in the *Yellow Cab Co.* case, *supra*, should have gone one step further and applied a discount factor to arrive at the *present worth* of the bonus or market value of \$6,434.40 as a lump sum payable *in praesenti*. Notwithstanding this technical objection, the decision represents a simplified mathematical approach to the problem and is a good working example of the valuation process.¹¹

It was held in *United States v. Certain Lands in the Borough of Brooklyn, County of Kings, State of New York*¹² that in a condemnation proceeding the claim of a tenant is for the market value of the unexpired term and a month-to-month tenant was not entitled to any award since there was no unexpired term.

In *People v. Klopstock*¹³ it was held that a tenant's assignment of a lease in violation of the provisions against assignment without the landlord's consent did not of itself terminate the lease or render the assignment void, and, where the landlord did not declare a forfeiture, the assignee's ultimate transferee was entitled to participate in the award for condemnation of the leased premises.

In *John Hancock Mutual Life Ins. Co. v. U. S.*¹⁴ the appellant complains of certain instructions given by the court. The court says:

"At the trial, the District Court instructed the jury that it could award damages to the appellant only if the fair market rental of the premises in question exceeded the rent that appellant was paying on the day it vacated and then only to the extent that the fair market rental exceeded the amount

¹¹Carlock v. United States, 53 F.2d 926 (D.C. Cir. 1931); 4 NICHOLS, THE LAW OF EMINENT DOMAIN § 12.42(3) (3d ed. 1951).

¹²39 F.Supp. 91 (E.D. N.Y. 1941).

¹³24 Cal.2d 897, 151 P.2d 641 (1944).

¹⁴155 F.2d 977 (1st Cir. 1946).

of the rent under the lease. The jury found that appellant was not entitled to damages. Appellant contends that the instruction of the trial court on the question of damages was erroneous in that it is entitled to the fair rental value undiminished by the rent it was obligated to pay under the lease. The correctness of that instruction is the sole question presented to us. . . . There was no error in the instructions of the court below."¹⁵

The principles deducible from the cases of many jurisdictions and from the text writers support the conclusion that where the entire remaining interest of a tenant under a lease is taken the damages payable to the tenant are measured by the market or bonus value, if any, of the unexpired term.

Elements of Compensation

We turn now to a consideration of the second important problem under the general subject of the value of leasehold interests. That question deals with the right of the lessee to be compensated for fixtures and other improvements installed by him upon the leased property, and the right to be compensated for other elements of claimed damage.

Generally speaking, a lessee is entitled to compensation for fixtures, structures, or other improvements installed or erected by him upon property taken under eminent domain, if, as against the lessor, he has the right to remove such improvements prior to or upon expiration of his term.¹⁶

Conversely, it has been held that a lessee is not entitled to compensation for fixtures or other improvements placed by him upon the condemned premises if, as against the lessor, he did not have the right to remove such improvements.¹⁷ Illustrative of this point is the case of *In re Triborough Bridge, City of New York*,¹⁸ wherein it was held that a tenant was not entitled to an award for a sprinkler system it had installed in the condemned building pursuant to the terms of the lease where the lease gave the tenant no right to remove the sprinkler system at the termination thereof; it appeared that the court must have taken the sprinkler system into consideration when determining the damage suffered by the owner of the building.

Again, in the case of *In re City of New York (Woolhiser)*¹⁹ a tenant was held not entitled to an award for light outlets and power circuits installed by him in the condemned building, the court saying that when these were imbedded in the building, they lost their character either as personalty or

¹⁵*Id.* at 978.

¹⁶*People v. Klopstock*, 24 Cal.2d 897, 151 P.2d 641 (1944); *City of Ladue v. St. Louis Public Service Co.*, 168 S.W.2d 966 (1943); *State of Nebraska v. Platte Valley Public Power and Irrigation District*, 147 Neb. 289, 23 N.W.2d 300 (1946).

¹⁷*United States v. Certain Lands in Jo Daviess Co., Ill.*, 120 F.2d 561 (7th Cir. 1941); *Corrigan v. City of Chicago*, 144 Ill. 537, 33 N.E. 746 (1893); *Baltimore v. Gamse & Bros.*, 132 Md. 290, 104 Atl. 429 (1918); *McAllister v. Reel*, 59 Mo.App. 70 (1894).

¹⁸249 App.Div. 579, 293 N.Y.Supp. 223 (1937).

¹⁹250 App.Div. 197, 293 N.Y.Supp. 850 (1937).

as trade fixtures, and became part of the realty for which full compensation presumably had been made to the owner of the realty.

Again, in *In re City of New York (North River)*²⁰ a lessee was held not entitled to compensation for improvements made by him, such as wiring, piping, a cold storage plant, and machinery, all of which were annexed to the building in such a manner as would render them valueless except for a use connected with the building, the court finding that such items did not constitute trade fixtures which could be removed by the tenant.

There is a line of cases, however, which hold that although upon the condemnation of leased premises the lessee may not be entitled to compensation for fixtures or other improvements installed or erected by him inasmuch as he does not have the right of removal, the cost of such improvements may be an element to be considered in determining the value of his leasehold interest.²¹

This theory is exemplified by the holding in *Carlock v. United States*,²² where the court held that expenditures by a tenant for years for improvements on the condemned premises, which under the terms of the lease became part of the realty, were entitled to be considered in determining the market value of the lease, the court saying that this did not mean that the lessee was entitled to compensation for the cost of the improvements, but only to the extent that they had enhanced the market value of the lease over and above the obligations of the lease, and to that extent they became an item of value to be considered in fixing the value of the lease.

In *United States v. 40.558 Acres of Land in New Castle County*²³ the court held that an expenditure by a lessee of \$2,000 for improvements to stables and dairies on a farm was a proper element to be considered in determining the fair market value of the leasehold estate at the time the property was condemned by the government.

Another vexing problem confronting the lawyer and appraiser is the determination of what shall be deemed personalty and what shall be deemed realty in a controversy between the tenant and the condemnor.

In *People v. Klopstock* it was held that fixtures are to be regarded as "personalty" as between the tenant and the owner of the land so far as the right of removal is concerned; but, as between the tenant and the con-

²⁰101 App.Div. 527, 92 N.Y.Supp. 8 (1905).

²¹*Carlock v. United States*, 53 F. 2d 926 (D.C. Cir. 1931); *United States v. Certain Parcels of Land in City of San Diego, Cal.*, 54 F.Supp. 561 (S.D. Calif. 1944); *United States v. 0.64 Acres of Land in Los Angeles County et al.*, 54 F.Supp. 562 (S.D. Calif. 1944); *United States v. 40.558 Acres of Land in New Castle County, Del.*, 62 F.Supp. 98 (D. Del. 1945); *Corrigan v. City of Chicago*, 144 Ill. 537, 33 N.E. 746 (1893); *Bales v. Wichita Midland Valley Railroad Co.*, 92 Kan. 771, 141 Pac. 1009 (1914); *Mayor of Baltimore v. Gamse & Bros.*, 132 Md. 290, 104 Atl. 429 (1918); *Bank of Brule v. Harper*, 141 Neb. 616, 4 N.W.2d 609 (1942); *North Coast Railroad Co. v. Kraft Co.*, 63 Wash. 250, 115 Pac. 97 (1911).

²²53 F.2d 926 (D.C. Cir. 1931).

²³62 F.Supp. 98 (D. Del. 1945).

demning party, they are regarded as part of the "realty" for the purpose of making compensation *so long as they remain fixtures*, and where, by the exercise of the right of eminent domain, they are destroyed or injured in value damages may be recovered therefor by the tenant.

It was held in *City of Los Angeles v. Hughes*²⁴ that nursery stock of the lessee planted upon the premises taken in eminent domain proceedings, under a stipulation in the lease that nursery stock might be grown upon the premises by the lessee for resale, was in the nature of an improvement for which the lessee was entitled to be compensated. The court said:

"It has often been held that property affixed to land which, as between the parties shall be deemed to be personal property, still retains its natural character of realty as to third persons."²⁵

It is said in the case of *City of Los Angeles v. Klinker*²⁶ that in condemnation proceedings the relation between the parties is regarded as similar to that of vendor and purchaser in determining the presence of irremovable fixtures.

It appears that the rule permitting the tenant to remove fixtures from the demised premises at the end of the term is entirely for the protection of the tenant and cannot be invoked by the condemnor. In condemnation cases where the question of what has become a part of the realty is involved the cases seem to lay great stress upon the intent with which a tenant has placed what were originally chattels on the property in spite of the fact that the condemnor manifestly could not have been a party to such intent.²⁷ As a general rule, therefore, when the lessee has a right—whether by operation of law or by agreement of the parties—to remove the improvements at the end of the term this right does not inure to the benefit of the condemnor and so permit the condemnor to treat the annexations as personalty outside the scope of the taking.²⁸

As a result, the ordinary rules applicable between landlord and tenant respecting the character of annexation do not apply in a controversy between the tenant and the condemnor. The rules applicable between vendor and vendee must be resorted to in order to determine what annexations are so affixed to the realty as to become part thereof and consequently pass with a conveyance of the freehold.

When the nature of the annexations are thus determined and found to be realty they must be paid for by the condemnor; but if the tenant had, as

²⁴202 Cal. 731, 262 Pac. 737 (1927).

²⁵*Id.* at 737, 262 Pac. at 740.

²⁶219 Cal. 198, 25 P.2d 826, 90 A.L.R. 148 (1933).

²⁷*People v. Church*, 57 Cal.App.2d 1032, 136 P.2d 139 (1943).

²⁸*United States v. Seagren*, 50 F.2d 333 (D.C. Cir. 1931); 4 NICHOLS, THE LAW OF EMINENT DOMAIN § 13.121(1) (3d ed. 1951).

against the landlord, the right to remove them, then the tenant and not the landlord is entitled to the compensation paid therefor.²⁹

A good illustrative case is *United States v. Seagren*,³⁰ where the court uses some interesting language in disposing of the contention of the United States.

In that case the United States was condemning a leasehold interest of the defendant who under the lease had erected and operated a gas station together with appurtenances thereto. In the condemnation proceeding the tenant made no claim in respect to any unexpired term on the theory that since his obligation was to pay only a reasonable rental, which had never been fixed as between him and the landlord, there was no ascertainable value in his term over the obligations of the lease. But he did assert a right to the reasonable value of his structures upon and within the land taken. The United States contested this claim on the ground that the tenant's right of removal reserved in the lease as against the landlord precluded his recovery in condemnation as against the United States. The court in rejecting this contention of the United States in respect to the pumps and tanks and other appurtenances, including the building which had been installed and erected upon the leased premises by the tenant, says:

"And so the agreement for removal made by these parties at another time, for another purpose, and affecting no interests but their own, must be rejected here as irrelevant, when set up by the United States to control its condemnation proceedings against the tenant's interest in the land. . . . The United States contends that the tenant here has lost nothing by the taking of the property.

"He reserved the right to remove his structures whenever the landlord should terminate his tenancy; now that the United States has terminated his tenancy by taking the land, he may exercise his right and remove his structures.

"Nothing has been taken from him. Only his performance of an inevitable obligation has been accelerated.

"But *much the same argument could be made in support of murder, for all that any murderer ever did was to accelerate the debt that every mortal owes to nature.*

"If the structures here in question had been built by the landlord, they would have been taken and paid for by the government without question, as the government concedes they are now part of the realty. Is the tenant's reserved power of removal as against the landlord's termination of the lease to work a forfeiture in favor of the government? We think not.

"The inherent character of these structures is real estate; no agreement can change that character, though the landlord may waive the right which might otherwise accrue to him from the character of the structures placed upon his land. At the most, that is all that this agreement did." (Emphasis added.)

²⁹In re Whitlock Avenue in City of New York, 278 N.Y. 276, 16 N.E.2d 281 (1938); 18 Am.Jur., Eminent Domain § 254; 29 C.J.S., Eminent Domain § 175 (b).

³⁰50 F.2d 333 (D.C. Cir. 1931).

It is obvious, of course, that if the tenant with a right to remove fixtures as against the landlord actually does so with the result that the condemnor does not physically take them, the tenant has elected to treat those fixtures as personal property and by severing them is estopped to claim compensation. The condemnor is manifestly not required to pay for what it does not take.

Conversely, where the tenant does not so elect, assuming he has that right, then we must resort to the vendor-vendee rules to determine whether the annexations are, in law, real or personal property to determine whether the condemnor is under an obligation to pay compensation therefor.

If we conclude that the annexations are realty then the tenant would be entitled to the award if he has the right of removal, otherwise the award for the annexations would belong to the landlord.³¹

The case of *United States v. Seagren* would seem to be in line with *In re Post Office Site*,³² which had held, with respect to an owner in fee, that in condemnation proceedings the rule which obtains in determining the property for which the condemnor shall give compensation is analogous to the rule that obtains between vendor and vendee, rather than that which obtains between landlord and tenant. In other words, if the improvement is such as would pass to a vendee under a contract of sale, the condemnor must pay for it.

Even where the lease contains a condemnation clause which is effective to deny the tenant compensation for the value, if any, of the unexpired term, the tenant would still retain his right to compensation for such fixtures which under the vendor-vendee rules would be regarded as part of the realty. This right, of course, assumes that as against the landlord the tenant has the right of removal at the end of the leasehold term.³³

It is clear that injury to the business of a lessee of premises taken or damaged by eminent domain is not compensable as an element of damage.³⁴ Nor are expenses incurred by a lessee in removing his personal property from the leased premises because of condemnation recoverable as an element of damage.³⁵

In the case of *United States v. Meyers*³⁶ it was held that tenants were not entitled to recover special damages on account of the cost of removing their fixtures to a new location, nor for loss of profits during such removal.

³¹*United States v. 40,379 Square Feet of Land, More or Less, in the City of Newton, Middlesex County, Mass.*, 58 F.Supp. 246 (D. Mass. 1944); *In re Triborough Bridge Approach, City of New York*, 159 Misc. 617, 288 N.Y.Supp. 697 (1936).

³²210 Fed. 832 (2d Cir. 1914).

³³*Matter of City of New York*, 192 N.Y. 295, 84 N.E. 1105 (1908); *In re Willcox*, 165 App.Div. 197, 151 N.Y.Supp. 141 (1914); *Matter of City of New York*, 256 N.Y. 236, 176 N.E. 377 (1931).

³⁴*City of Oakland v. Pacific Coast Lumber and Mill Co.*, 171 Cal. 392, 153 Pac. 705 (1915).

³⁵*People v. Auman*, 100 Cal.App.2d 262, 223 P.2d 260 (1950); *Los Angeles County v. Signal Realty Co.*, 86 Cal.App. 704, 261 Pac. 536 (1927).

³⁶190 Fed. 688 (D.C. Cir. 1911).

It was said in the case of *In re Petition of New York and Brooklyn Bridge*:³⁷

"The measure of damages in cases of this character [taking of leasehold interests] is well settled to be the value of the unexpired term of the lease, less the rent reserved. The tenant is not entitled to be awarded damages caused by the necessity of removal of personal property, nor consequential damage arising from interruption of business."³⁸

So far as strictly personal property is concerned, the rule is set out in Nichols, *The Law of Eminent Domain*:³⁹

"A taking of real estate does not affect the ownership of personal property kept on the premises taken, but not affixed thereto. Thus, the owner is entitled to remove such property. Personal property which is used on land taken by eminent domain cannot be considered in the determination of the compensation."

Following the general condemnation rule, it has been held in a number of cases that a tenant's loss of business, profits, good will and costs of removal from the premises are not elements of damage awardable in condemnation proceedings which are proceedings *in rem*.⁴⁰

To many laymen, especially when they find themselves defendants in a condemnation proceeding, this refusal of the law to compensate for loss of business or profits comes as a distinct shock. Yet this loss, however real it may be, is not within constitutional protections and is not a subject of compensation in eminent domain. It is *damnum absque injuria*.⁴¹

The denial of compensation for claimed loss of business is grounded upon the basic legal concept that what is taken is the real property and not the business. Most courts feel that the profits derived from the conduct of a business do not even tend to prove the value of the property upon which it is conducted. It has been said that one man will get rich while another will become bankrupt in conducting the same business upon the same property.⁴²

Evidence of profits derived from a business conducted on the property have been held too speculative, remote and uncertain to be considered as a basis for computing or ascertaining the market value of property in condemnation proceedings.⁴³

It has been said that injury to a business is a detriment to its owner

³⁷50 Hun. 606, 4 N.Y.Supp. 222 (1888).

³⁸*Ibid.*

³⁹4 NICHOLS, *THE LAW OF EMINENT DOMAIN* § 13.13 (3d ed. 1951).

⁴⁰*United States v. General Motors Corp.*, 323 U.S. 373, 65 S.Ct. 357, 89 L.Ed. 311, 156 A.L.R. 390 (1944); *People v. Ricciardi*, 23 Cal.2d 390, 396, 144 P.2d 799 (1943); *Morris v. City and County of San Francisco*, 59 Cal.App. 364, 210 Pac. 824 (1922); *City of Long Beach v. Wright*, 134 Cal.App. 366, 25 P.2d 541 (1933); *City of Los Angeles v. Geiger*, 94 Cal.App.2d 180, 210 P.2d 717 (1949); *City of Newark v. Cook*, 99 N.J.Eq. 527, 133 Atl. 875 (1926); *In re Petition of New York and Brooklyn Bridge*, 50 Hun. 606, 4 N.Y.Supp. 222 (1888).

⁴¹*Morris v. City and County of San Francisco*, 59 Cal.App. 364, 210 Pac. 824 (1922).

⁴²2 LEWIS, *EMINENT DOMAIN* § 727.

⁴³*State v. Cerruti*, 188 Or. 103, 214 P.2d 346 (1949).

but not a damage to the property on which it is conducted.⁴⁴ A particular business might be entirely destroyed and yet not diminish the actual value of the property for its highest and best use.⁴⁵

The business is something entirely distinct from the market value of the land on which it is conducted and cannot be considered except insofar as it illustrates one of the uses to which the land itself is adapted.

It has often been argued that this is a harsh rule and that the injury in many cases is real and permanent. If the rule were otherwise, however, untold sums would be disbursed by condemning agencies in payment of claims for loss of business, many of which undoubtedly would be fraudulent and many more grossly inflated. The practical difficulties in fairly appraising such a loss are obvious. The possibility that any given property may someday be acquired by eminent domain with consequent injury or destruction of the business conducted thereon is one of the inherent risks of ownership and one of the hazards of capital investment. It may remain an open social and economic question as to whether the loss should fall upon the public or the risk-takers. The law, however, up to this point, has decided in favor of the public.

It may well be that one day insurance companies will find that coverage of this risk is but a short step from business interruption insurance and may make available a policy to protect the businessman against business loss resulting from an eminent domain proceeding. In attempting to frame such a policy and to define its limits the actuaries, statisticians and lawyers will be embarking upon a valuation problem which will probably prove to be as interesting as it will surely be exasperating. Such insurance coverage appears to be a realistic answer. The business community in general, through the pool of premiums, would be sharing and distributing the risk and underwriting the loss which is certain to be visited upon an actuarially ascertainable number of its members in a given period of time.

An interesting case is that of *Fiorini v. City of Kenosha*,⁴⁶ which was a condemnation action in which the lessee took an appeal from certain rulings of the court below. The lessee had a lease expiring on September 21, 1931, at a rent of \$175 per month. About May 1, 1928, the tenant was notified by the city to vacate the premises by May 1, 1929. He then rented a place on the opposite side of the street for \$350 per month as a location in which to carry on his meat market business. He moved into the new store on October 1, 1928. He moved his fixtures into the new location. They did not fit and an ice machine so moved for some reason became useless and valueless. He claims his business in the new location was less profitable than in

⁴⁴*City of Los Angeles v. Geiger*, 94 Cal. App. 2d 180, 210 P.2d 717 (1949).

⁴⁵*People v. Ricciardi*, 23 Cal.2d 390, 144 P.2d 799 (1943).

⁴⁶208 Wis. 496, 243 N.W. 761 (1932).

the old and claims as damages depreciation in the value of his fixtures, loss of profits, etc. He offered to prove such depreciation and loss of profits, but objection thereto was sustained on the ground that they did not constitute elements of damage. The Supreme Court of Wisconsin, in passing upon these contentions, says:

"We are of the opinion that there was no error in rejecting evidence of loss of profits.

"It is stated in 2 Lewis on Eminent Domain, § 488, that damages to personal property or the expense of removing it cannot be considered in estimating damages for the taking of land by condemnation. That depreciation of a lessee's fixtures is not an element of damage in condemning his leasehold is held in *Des Moines Wet Wash Laundry v. Des Moines, etc.*, supra [197 Iowa 1082], 198 N.W. 486; *Shipley v. Pittsburgh, etc., Ry. Co.*, [216 Pa. 512] 65 Atl. 1094; *Kersey v. Schuylkill River E.S.R. Co.*, [133 Pa. 234] 19 Atl. 553; *Ranlet v. Concord Ry. Corp.*, 62 N.H. 561; *Bales v. Wichita Midland Ry. Co.*, supra [92 Kan. 771], 141 Pac. 1009. By these cases, however, the fixtures placed on the premises by the lessee and their value may be shown as affecting the value of the lessee's term. As there was here no evidence offered as to the value of the remainder of the term, and the evidence was offered to establish an item of damages, there was no error in rejecting it.

"No condemnation cases are called to our attention in which expenditures in mitigation of damages have been allowed or claimed. In view of the general rule as to the measure of damages in such cases, which is the difference between the values of the property affected before and after the taking, we do not perceive any reason for receiving expenditures in evidence. Expenses of removing personal property cannot be considered. 2 Lewis on Eminent Domain, § 488. Such expenditures not being recoverable, we see no reason why expenditures to secure a new location or to prevent loss of trade should be. All such items of expenditure and depreciation of fixtures and other personal property as well are incident to removal from the premises at the end of the term of the lease. No recovery lies for them on the expiration of a lease. No more should recovery for them be allowed on termination of occupation caused by condemnation of part of the leased property."⁴⁷

It has sometimes happened, especially in war-time condemnations by the Federal Government, that less than the entire remaining leasehold term is condemned. For example, a lease may have ten years to run and the government condemns a five-year term. The tenant is then left with the last five years under the lease. This fact situation forms an exception to certain principles of compensation heretofore discussed. *United States v. General Motors Corp.*⁴⁸ is a representative example. There the lease extended beyond the period of the government's taking. The court found that in such a special situation there is imposed upon the tenant the onerous burden of moving out, and if it is to fulfill its obligation, later moving back. Hence, moving costs

⁴⁷*Id.* at 498, 499, 243 N.W. at 762.

⁴⁸323 U.S. 386, 65 S.Ct. 373, 89 L.Ed. 322 (1945).

and the value of fixtures destroyed or depreciated are allowed in such cases.⁴⁹

In the ordinary case the sovereign takes the whole interest of the tenant. Compensation does not include consequential losses, moving expenses, loss of business or loss of goodwill. In the taking of temporary occupancy under a long term lease, however, the courts have worked out exceptions to the usual rules. These situations call for special legal and appraisal treatment.

So far we have been considering those special and exceptional cases where the condemnor seeks to take the interest of the tenant only. It is assumed that the condemnor has either settled or litigated with the fee owner for his interest or is concerned only in condemning a leasehold interest for its own occupancy.

In actual practice where the government seeks to acquire a site for a public building or as part of a highway construction program it normally proceeds against all interests in the property at the same time in an *in rem* proceeding and in that proceeding acquires the title of all owners, lessees and lienholders. The total of all these subordinate interests adds up to the entire unencumbered fee.

When this procedure is followed the legal and appraisal problems are easier of solution for the property is treated as though held by one owner regardless of how many subordinate interests or estates might have been carved out of the fee.

In *Carlock v. United States*⁵⁰ the court says:

"It is a fundamental principle, governing condemnation proceedings, where several interests are involved, such as estates for life, or in remainder, or leaseholds, or in reversion, in the property to be condemned, all should be combined in determining the value of the fee, after which the total value of the fee can be subdivided in satisfaction of the values fixed upon the various interests involved."⁵¹

In the case of *United States v. 25.936 Acres of Land*⁵² the court employs this language:

"It is settled that when land in which various persons have separate interests or estates is taken by the United States for public use, the amount of compensation to be paid must be determined as if the property was in single ownership and without reference to conflicting claims or liens. See *Meadows v. United States*, 4 Cir., 144 F.2d 751, 752, 753; *United States v. 576.734 Acres of Land*, 3 Cir., 143 F.2d 408, 409. The compensation paid is for the land itself and the value of the separate interests cannot exceed the worth of the whole. See 2 Lewis, *Eminent Domain*, 3d Ed., p. 1253; 1 Nichols, *Eminent Domain*, 2d Ed., pp. 707, 708.

⁴⁹*United States v. Petty Motor Co.*, 327 U.S. 372, 66 S.Ct. 596, 90 L.Ed. 727 (1945); *United States v. Westinghouse Co.*, 339 U.S. 261, 70 S.Ct. 644, 94 L.Ed. 816 (1949); *United States v. 5.42 Acres of Land, More or Less, Situate in Atlantic City, Atlantic County, N. J.*, 182 F.2d 787 (3d Cir. 1950).

⁵⁰53 F.2d 926 (D.C. Cir. 1931).

⁵¹*Id.* at 927.

⁵²153 F.2d 277 (3d Cir. 1946).

"A condemnation proceeding is a proceeding in rem. It is not a taking of rights of persons in the ordinary sense but an appropriation of the land or property itself. As indicated by the Supreme Court in *Duckett & Co. v. United States*, 266 U.S. 149, 151, 45 S.Ct. 38, 69 L.Ed. 216, all previous existing estates or interests in the land are obliterated."⁵³

The case of *City of St. Louis v. Rossi*⁵⁴ is one of the leading decisions in the United States and has often been quoted by the United States Supreme Court as establishing the principles which follow:

"The well established general rules of eminent domain seem to be that, when a piece of property is taken, in which the ownership is divided into several interests, as between the public and the owners, it is considered one estate; that the public right is exercised upon the land itself without regard to the subdivisions of interest; that the amount of the value of the land to which each one of the owners of the interests is entitled is no concern of the condemnor; that the various owners' interests in the property are transferred to the fund, allowed as damages to compensate them for the injury to the land, which is substituted for the property taken; that the value of the property taken is all that the condemnor must pay, and this value cannot be increased by any contracts or distribution among the different persons owning interests in it; and that the sum of all the parts cannot exceed the whole." (Citing cases.)⁵⁵

The California Code of Civil Procedure embodies the rule of these cases.⁵⁶

After the entire compensation has been determined as though the property were held by one person, then the award is apportioned among the different claimants according to their respective rights. This procedure appears fair and equitable to all concerned since it is clear that no distribution of the title or estate among different owners can enhance the value of the property. The sum of the parts cannot exceed the whole, and the advantage which may accrue to one interest must be taken from another.

The total amount of damages must be the same whether the land is owned by one person or several.⁵⁷

It is said in *In re Daly*:⁵⁸

"The city is not bound to make greater compensation for all the combined interests in the land taken than the full value of the fee."⁵⁹

The case of *Meadows v. United States*⁶⁰ involved the taking of timber

⁵³*Id.* at 279.

⁵⁴333 Mo. 1092, 64 S.W.2d 600 (1933).

⁵⁵*Id.* at 1102, 1103, 64 S.W.2d at 604.

⁵⁶See note 1 *supra*. See, also, *United States v. Block*, 160 F.2d 604 (9th Cir. 1947); *Thibodo v. United States*, 187 F.2d 249 (9th Cir. 1951); *People v. Buellton Development Co.*, 58 Cal.App.2d 178, 136 P.2d 793 (1943).

⁵⁷State ex rel. *Youngquist v. Anderson*, 176 Minn. 525, 223 N.W. 923 (1929); 2 LEWIS, EMINENT DOMAIN § 716.

⁵⁸29 App.Div. 286, 51 N.Y.Supp. 576 (1898).

⁵⁹*Id.* at 287, 51 N.Y. Supp. at 577.

⁶⁰144 F.2d 751 (4th Cir. 1944).

land in North Carolina by the federal government for a Marine Corps air base. The appellant, Sara Meadows, was the owner of the fee, subject to a deed to appellant, Taylor, for the timber on the tract, of and above the size of 10 inches in diameter, measured 12 inches above the ground, and there were other encumbrances upon the land. The question was whether the defendants (appellants) were entitled to separate trials as to the value of their holdings. The court said:

" . . . We are of the opinion that the judge below was correct in holding that in this proceeding the Government was entitled to have the value of the property, as a whole, fixed by the jury. The Government was seeking to take the property for a lawful use and was not interested in conflicting claims of owners as to the value of their respective interests. The taking was not of the rights of designated persons in the property but of the property itself. . . . The value of the property once being determined in a proper proceeding, the sum so determined stands in the place of the property and can be distributed upon the adjudication of the value of the respective interests. *United States v. Dunnington*, 146 U.S. 338, 13 S.Ct. 79, 36 L.Ed. 996; *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 13 S.Ct. 622, 37 L.Ed. 463."⁶¹

Once the total amount of compensation is fixed the condemnor has no further interest in the proceeding so far as the apportionment is concerned. The problem now becomes one of determining the worth of the respective interests in the property and dividing up the total award on the basis of the value of those interests. The case of *City of Pasadena v. Porter*⁶² is illustrative of such a proceeding. That case involved the taking of part of a parcel of improved property which was under lease. An award was made in a lump sum for compensation and damages, which was later apportioned between the lessor and lessee. Since only a part of the leased premises was taken the lessee remained under a continuing obligation to pay the full rent. (Note the dissenting opinion in which Mr. Justice Curtis expresses the view that in cases of partial taking of leased premises there should be a pro rata reduction in rent under the lease.)

The California Supreme Court affirmed the judgment of the lower court which found, in addition to a bonus value in the lease, that the lessee was entitled to a further sum which, invested at 6 per cent interest and drawn on at the rate of \$166 per month for the remainder of the leasehold term, would exactly reimburse the tenant for the portion of the rent attributable to the condemned part of the leased premises. Although this portion of the property was no longer enjoyed by the tenant he remained under an obligation to pay full rent for the condemned portion. The sum provided, both principal and interest, would be exhausted upon the last payment of \$166 for the last month of the lease.

⁶¹*Id.* at 752, 753.

⁶²201 Cal. 381, 257 Pac. 526, 53 A.L.R. 679 (1927).

It surely seems that the better rule would be that contended for in the dissenting opinion. A pro rata reduction in rent would accomplish the identical result without resort to complicated mathematical calculations. Under the *City of Pasadena v. Porter* rule the landlord is in a position of greater risk since, in effect, the tenant is holding for the landlord a fund payable in installments which really represents a deferred payment for a part of that landlord's reversionary interest. If the tenant defaults or becomes insolvent before making all payments from the fund, the landlord may never recoup his loss. Even if he re-let for the account of the defaulting tenant, the monthly rental he could expect to receive from a new tenant would be less than the defaulting tenant was paying under this artificial arrangement for the simple reason that the new tenant would pay rent only for the premises which he could use and enjoy, assuming no change in rental values. The extra \$166 per month represents payment for premises no longer in existence.

Despite argument to the contrary the rule of *City of Pasadena v. Porter* is the law and lawyers and appraisers must continue to live with it.

From this cursory review of but one phase of eminent domain valuation it can be seen that the field is wide and complex. More and more practitioners are daily coming into contact with condemnation actions. The public necessities of our present population and economy require more frequent exercise of the power of eminent domain by governments and their subordinate agencies as well as by public and private corporations. A thorough analysis of each case on its fact, law and valuation aspects is essential, for the lawyer must tell the appraiser, no matter how experienced the appraiser may be in his own field, what elements of actual damage are recognized as compensable and what elements are not. Only by close cooperation between lawyer and appraiser—each working in his own field—can valuation evidence be obtained which will safely and legitimately pass through the jungle of rules and court decisions which have been developing through the course of centuries and which are daily becoming more numerous as the ancient and essential power of eminent domain continues to be invoked.